

# **RATE REGULATION:**

**HOW ITS UNINTENDED  
CONSEQUENCES COULD  
GREATLY HARM PROGRAM  
SERVICES**

## **CURRENT IMPACT ON DCI DUE TO THREAT OF RATE REGULATION**

- **TLC LAUNCHES ARE STALLED AS OPERATORS AWAIT RE-REGULATION AND REFUSE TO LAUNCH ANYTHING MORE ON BASIC**
- **OPERATORS SAY "BASIC IS DEAD" "WE HAVE TO TIER YOU" BECAUSE WE CAN'T PASS ON COSTS IF WE ADD YOU TO BASIC**
- **AS OPERATORS MAKE ROOM FOR MUST CARRY, THEY USE UP CHANNELS AND CAN'T LAUNCH TLC**
- **WE HAVE HAD TO DRAMATICALLY SCALE BACK OUR BUSINESS PLAN EXPECTATIONS FOR TLC. GOAL NOW 30-40M SUBS VS 60M & AN ASSET WORTH A LOT LESS THAN DISCOVERY**

# OUR PASSIONATE PLEA

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# **WHY BEING ON BASIC IS OPTIMAL**

- . Being on basic gives 100% of viewers in any market a chance of seeing your service**
- . Because basic carriage maximizes your sub volume, viewership and thus advertising revenue are maximized**
- . Consumers benefit: programming fee charged to affiliates, and ultimately consumers, is minimized**

## **WHY BEING ON A TIER SUB-OPTIMIZES**

- **In tiered world, subscribership and therefore viewership and ad revenue are limited; perhaps greatly limited**
- **Subscribership is limited because only a percentage choose to pay the extra fee**
- **Viewership is limited because there is a smaller pool who can choose to view any given network**
- **Ad revenue is limited because subscribership and viewership are limited**
- **Marketing costs are greatly increased because of the expense of promoting yourself to subs**
- **Because of reduced ad and subscriber revenues and greater marketing costs, consumers pay more.**

## THE ECONOMICS TO A PROGRAMMER OF BEING CARRIED ON BASIC VS. BEING CARRIED ON TIER

### ASSUMPTIONS:

- A network is carried by affiliates servicing 20 million "basic" households.
- Total annual expenditures for the network amount to \$50 million.
- In order to hit financial "break-even", the network must be able to achieve ad plus affiliate revenues totaling \$2.50 per "basic" household ( $\$2.50 \times 20 \text{ million}$ ).
- For every household that the network is in, \$1.25 of ad revenue is expected to be earned (assuming viewership estimates are achieved).

## OTHER PROBLEMS CAUSED BY TIERS:

REDUCTION IN SAMPLING UNIVERSE NEGATIVELY AFFECTS RATINGS.

ADVERTISERS WILL PAY US LESS IF THEY GET A "PORTION" OF ALL THE MAJOR MARKETS (20-30%) VERSUS ALL OF THE MAJOR MARKETS.

PERCEPTION OF GROWTH AND MOMENTUM IS VITAL TO ADVERTISERS. ON TIERS, GROWTH IS GREATLY SLOWED.

TIERS ARE EXTREMELY CONFUSING TO CONSUMERS.

MARKETING TENDS TO SOUND LIKE A DIABETIC SOLD

## **PROBLEMS WITH TIERS CONTINUED....**

**OUR BUSINESS PLANS CANNOT ABSORB THE HIGH COSTS OF THE CONSTANT MARKETING THAT'S NECESSARY.**

**ADVERTISING IS A MULTI-LEVELED SALE. LOTS OF PEOPLE HAVE TO BELIEVE IN YOUR NETWORK. BUT ADVERTISERS ARE VIEWERS TOO. IF THEY CAN'T SEE YOUR CHANNEL THEMSELVES, YOU DON'T EXIST. THEY WON'T "VOTE" FOR YOU TO BE INCLUDED IN A BUY.**



## ANALYSIS OF AFFILIATE FEE PRICING BASED ON DIFFERENT TIERING LEVEL SCENARIOS:

| NETWORK<br>PENETRATION | NETWORK<br>SUBSCRIBERS* | ANNUAL AD<br>SALES<br>(@\$1.25/SUB) | REQUIRED SUB<br>REVENUE (FOR<br>"BREAK-EVEN") | REQUIRED<br>SUBSCRIBER<br>FEE/MONTH |
|------------------------|-------------------------|-------------------------------------|---|-------------------------------------|
| 100%                   | 20 MILLION              | \$25 MILLION                        | \$25 MILLION                                  | 10.0¢                               |
| 80%                    | 16 MILLION              | \$20 MILLION                        | \$30 MILLION                                  | 16.0¢                               |
| 60%                    | 12 MILLION              | \$15 MILLION                        | \$35 MILLION                                  | 24.0¢                               |
| 40%                    | 8 MILLION               | \$10 MILLION                        | \$40 MILLION                                  | 42.0¢                               |
| 20%                    | 4 MILLION               | \$5 MILLION                         | \$45 MILLION                                  | 94.0¢                               |

\*Out of 20 Million "Basic" Subs

*Handwritten signature/initials*

# RECAP

## **RECAP OF REASONS WHY DISCOVERY COMMUNICATIONS, INC. HAS DIFFERENTIATED IN PRICING TO ITS AFFILIATES**

1. **"CHARTER" AFFILIATES:** THE INITIAL GROUP OF AFFILIATES WHO ASSISTED THE NETWORKS BY AGREEING TO GIVE UP FREE CONTRACTS AND TO PAY A FEE. THEY DESERVE "SPECIAL" PRICING CONSIDERATION.
2. **"VOLUME" DISCOUNTS:** AFFILIATES THAT PROVIDE A GREATER QUANTITY OF SUBSCRIBERS MAKE A GREATER CONTRIBUTION TO NETWORK ADVERTISING AND AFFILIATE REVENUES AND THEREFORE DESERVE SPECIAL PRICING CONSIDERATION
3. **"LOW PENETRATION / TIERING" PENALTIES:** AFFILIATES AND THEIR SYSTEMS THAT PACKAGE OUR NETWORKS IN SUCH A WAY THAT THEY ACHIEVE LOW "PENETRATION" PAY A PENALTY (OR SURCHARGE). THE SURCHARGE IS INTENDED TO RECOVER LOST AD / AFFILIATE REVENUE AND INCENT RE-PACKAGING KEYED TO THE PERCENTAGE OF THEIR SUBSCRIBERS THAT RECEIVE THE SERVICE.
4. **HIGHER COST TO DELIVER, MARKET, OR SERVICE:** IF THERE ARE INCREMENTAL COSTS ASSOCIATED WITH PROVIDING SERVICE TO AN AFFILIATE OR GROUP OF AFFILIATES, THESE COSTS ARE RECOVERED THROUGH A HIGHER RATE PER SUB (E.G. TVRO, TIERS).
5. **STANDARDS/PRACTICES OF NON-VERTICALLY INTEGRATED PROGRAMMERS:** DCI HAS FOLLOWED PRACTICES USED BY NON-VERTICALLY INTEGRATED PROGRAMMERS, I.E., MARKET DRIVEN PRACTICES, BASING ITS TVRO RATE IN PART ON MARKET FACTORS.

**ESTIMATED REVENUE LOSS TO DISCOVERY IF "LOWEST UNIT" RATE IS ADOPTED:**

| 1993  | 1994  | 1995  | 1996  | 4 YEAR TOTAL |
|-------|-------|-------|-------|--------------|
| \$13M | \$12M | \$11M | \$10M | \$46M        |

**ESTIMATED REVENUE LOSS TO TLC IF TIERING PRICES ARE CONSTRUED TO BE DISCRIMINATORY:**

| 1993 | 1994 | 1995 | 1996  | 4 YEAR TOTAL |
|------|------|------|-------|--------------|
| \$0M | \$2M | \$5M | \$10M | \$17M        |

**TOTAL LOST REVENUE ESTIMATE:**

| 1993  | 1994  | 1995  | 1996  | 4 YEAR TOTAL |
|-------|-------|-------|-------|--------------|
| \$13M | \$14M | \$16M | \$20M | \$63M        |

# PROPOSED SOLUTIONS

## PROPOSED SOLUTIONS - PROGRAM ACCESS

- Presumption that pricing is not discriminatory or anti-competitive:
  - If programmer offers same rate card to alternate technologies (other than TVRO) as to cable affiliates
  - If rates to TVROs are under the average rate charged by non-vertically integrated programmers (less than 49¢)
- Create "safe harbor" for program services that serve 50% or more of SMATV, MMDC, TVRO and DBS (alternate technology) markets
- Grandfather existing contracts
- Create "safe harbor" for vertically integrated programmers whose practices closely parallel those of non-integrated programmers

# PROPOSED SOLUTIONS - RATE REGULATION

- ALLOW OPERATORS TO PASS THROUGH
  - NET CAPACITY EXPANSION COSTS
  - TECHNOLOGICAL IMPROVEMENT COSTS
  - PROGRAMMING COSTS

THESE PASS THROUGHES WILL ENCOURAGE INCREASED

# **General Information on Discovery Channel & e Learning Channel**



## Fast Facts

7700 Wisconsin Avenue  
Bethesda, MD 20814-3522  
301.986.1999

DISCOVERY COMMUNICATIONS, INC.



## FAST FACTS

**Discovery Communications, Inc. (DCI)** is a diversified multimedia company anchored by cable television's The Discovery Channel and The Learning Channel. DCI also operates businesses in home video, interactive multimedia, publishing, merchandising and international sales and distribution.

**Discovery Networks**, a division of Discovery Communications, Inc., manages and operates both The Discovery Channel and The Learning Channel. The Discovery Channel offers the finest in non-fiction entertainment to over 59 million U.S. households. The Learning Channel is the only cable network that consistently offers people of all ages -- from pre-schoolers on -- an enjoyable, entertaining way to learn and satisfy their natural curiosity.

### PARENT COMPANY:

Discovery Communications, Inc.

### HEADQUARTERS:

7700 Wisconsin Avenue  
Bethesda, MD 20814-3522  
(301) 986-1999 or (301) 986-0444 (Voice Mail)

### LAUNCH DATE:

The Discovery Channel  
June 1985  
  
The Learning Channel  
November 1980  
(Acquired by Discovery Communications in May 1991)

### SUBSCRIBERS:

The Discovery Channel: 59.4 million households  
(Nielsen Universe Estimate, March 1993)  
  
The Learning Channel: 19.5 million households  
(Nielsen Universe Estimate, March 1993)  
Does not include alternate technologies distribution

# DISCOVERY COMMUNICATIONS, INC.

(continued)

## EXECUTIVE COMMITTEE:

John S. Hendricks  
*Founder, Chairman and CEO*  
*Discovery Communications, Inc.*

Ruth L. Otte  
*President and COO*  
*Discovery Networks*

Gregory B. Moyer  
*Executive Vice President*  
*Programming Group*

Greg Durig  
*Senior Vice President and*  
*Chief Financial Officer*

Domenick Fioravanti  
*Senior Vice President*  
*Corporate Development*  
*and International*

Bill McGowan  
*Senior Vice President*  
*Advertising Sales*

Judith A. McHale  
*Senior Vice President*  
*Corporate Services*  
*and General Counsel*

Chris Moseley  
*Senior Vice President*  
*Marketing & Communications*

## PRESS CONTACTS:

Jim Boyle (ext. 5670)  
*Vice President*  
*Communications*

Susan Murrow (ext. 5432)  
*Director*  
*Programming Publicity*

Vicki Stearn (ext. 5436)  
*Senior Manager*  
*Communications*

Krista Van Lewen (ext. 5274)  
*Manager*  
*Corporate Communications*

DISCOVERY COMMUNICATIONS, INC.  
7700 Wisconsin Avenue | Bethesda, Maryland | 20814-3522  
(301) 986-1999 | (301) 986-4826 FAX

# FAST FACTS

## The Discovery Channel Fast Facts

**Programming:** The Discovery Channel is the only cable network to feature 18 hours a day of the world's finest non-fiction entertainment covering nature and the environment, science and technology, history, adventure and the people who share our world.

**Hours:** 9 AM to 3 AM ET (18 hours per day)

**Launched:** June 17, 1985

**Affiliates:** 9,731 cable systems in all 211 DMA's

**Subscribers:** 59.4 million (A.C. Nielsen as of March 1993)

**Satellites:** Satcom C-4, transponder 21 (East Coast)  
Galaxy 5, transponder 12 (West Coast)

**Ownership:** Cox Cable Communications; John S. Hendricks; NewChannels Corp.; and TCI Development Corp.

**Executives:** John Hendricks  
Founder, Chairman and CEO  
Discovery Communications, Inc.

Ruth Otte  
President and Chief Operating Officer  
Discovery Networks

# The Discovery Channel

(continued)

Gregory B. Moyer  
Executive Vice President  
Programming Group  
Discovery Communications, Inc.

Charles Gingold  
Senior Vice President  
Programming, TDC-USA

Dawn McCall  
Vice President  
Affiliate Sales and Relations  
The Discovery Channel

Chris Moseley  
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# FAST FACTS

## THE LEARNING CHANNEL

*The Learning Channel (TLC)* is the only cable network that consistently offers people of all ages -- from pre-schoolers on -- an enjoyable, entertaining way to learn and satisfy their natural curiosity. Relaunched October 1, 1991, this new *viewer friendly* service features stimulating, provocative non-fiction that awakens the power of the mind. *TLC* signature series and specials explore the humanities, arts, sciences, entertainment and much more that enriches and delights.

**PARENT COMPANY:** Discovery Communications, Inc.

**LAUNCH DATE:** November 1980  
(Acquired by Discovery Communications in May 1991)

**RE-LAUNCH:** October 1, 1991

**AFFILIATES:** 1522 cable systems in top 100 DMA's

**SATELLITE:** Satcom C-3, transponder 2

**SUBSCRIBERS:** 19.5 million households  
(Nielsen Universe Estimate, March 1993)  
Does not include alternate technologies distribution.

**EXECUTIVES:** John Hendricks  
*Founder, Chairman and CEO*  
*Discovery Communications, Inc.*

Ruth Otte  
*President and COO*  
*Discovery Networks*



# THE LEARNING CHANNEL

(continued)

Gregory B. Moyer  
*Executive Vice President*  
*Programming Group*  
*Discovery Communications, Inc.*

John B. Ford  
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# FAST FACTS

## HISTORICAL HIGHLIGHTS

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**1985**

June 17

With financial backing from New York Life Insurance, Allen and Company Inc., and Group W Satellite Communications, The Discovery Channel, headed by founder, Chairman and CEO John Hendricks, launches on Galaxy 1 satellite, transponder 22, with approximately 156,000 subscribers.

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**1986**

June

Four multiple system cable operators (MSOs) join previous backers in making an investment in The Discovery Channel. They are: United Cable Television Corp., Cox Cable Communications, Inc., Newhouse Broadcasting Corp., and Tele-Communications Inc.

|          |  |
|----------|--|
| February | Discovery, in association with Orbita Technologies Corporation, makes television history by broadcasting 66 hours of live Soviet television. <b>Russia: Live From the Inside</b> gives Americans their first glimpse of domestic Soviet television.                                    |
| June 17  | Discovery celebrates its second birthday announcing an unprecedented growth of 8.4 million subscribers for the first quarter of 1987, bringing subscriber base to 18.4 million (more than 100% growth over the previous year).   |
| July     | A.C. Nielsen begins to measure Discovery.  |
| December | Discovery enters agreement with Mitsubishi Corporation which allows the latter to telecast Discovery programming in Japan via cable television and closed-circuit TV.<br><br>Discovery ends the year with 27.5 million subscribers, representing a 170% growth over the previous year. |

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## 1988

|          |   |
|----------|---|
| January  | Discovery is named the 1987 Golden ACE Award Winner for <b>Russia: Live From the Inside</b> . |
| April    | Discovery is named the fastest growing cable television network in history by A.C. Nielsen.   |
| June 17  | Discovery celebrates its third anniversary with 32.1 million subscribers.                     |
| December | Discovery finishes the year with 38.1 million subscribers.                                    |

-Continued



# FAST FACTS

Discovery Communications, Inc.

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1989

January

Discovery is named the fastest growing cable television network for the second year in a row by A.C. Nielsen.

March

Discovery subscriber base passes the 40 million mark with 40.6 million households on line (Nielsen, March 1989).

Cox Communications, Inc., NewChannels Corp. and TCI Development Corp. purchase shares of Discovery previously held by Allen and CO., New York Life, Westinghouse and other non-MSO investors of the network.

April

Discovery launches The Discovery Channel - Europe to more than 200,000 homes in the United Kingdom and Scandinavia.

Discovery ranks among the top cable networks in non-subscriber interest in Beta Research Corp.'s national non-subscriber poll.

September

Discovery launches its educational initiative, **Assignment Discovery**, a one-hour weekday morning program designed to be taped by teachers for use in the classroom.

Discovery begins week-long tribute to Africa with **Safari Live! Africa Watch**, an unprecedented live transmission from Kenya's Masai Mara Game Reserve. The tribute continued with **Ivory Wars**, and concluded with **Student Safari** which provided a live audio and video link between students in a Washington, D.C. television studio and African wildlife experts in Kenya.

November

Discovery passes 50 percent penetration of all U.S. TV households with a subscriber count of 46.1 million homes.